



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

July 29, 2008

S. 3013

Non-Foreign AREA Act of 2008

*As ordered reported by the Senate Committee on Homeland Security
and Governmental Affairs on June 25, 2008*

SUMMARY

S. 3013 would phase in the use of locality-based comparability payments ("locality pay") to replace cost-of-living allowances (COLAs) for federal employees in certain areas of the United States (Alaska, Hawaii, and the U.S. Territories).

The bill would affect the amount of pay received by certain federal employees and the amount of future retirement benefits those employees receive. By increasing some salaries, S. 3013 would result in additional agency payments for employees' retirement benefits and payroll taxes. In total, CBO estimates that discretionary spending would increase by \$2.2 billion through 2018, assuming appropriation of the necessary amounts. The legislation also would increase the amount of pay included in the calculation of retirement and Social Security benefits, thereby increasing direct spending by an estimated \$302 million over the 2009-2018 period. Furthermore, including additional pay in the calculation of retirement benefits would increase revenues—from higher employee contributions towards those benefits and from additional tax receipts—totaling an estimated \$1 billion over the 2009-2018 period.

S. 3013 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no cost on state, local, or tribal governments.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 3013 is shown in the following table. The direct spending impacts of the bill fall within budget functions 600 (income security) and 650 (Social Security); the discretionary costs fall within many other budget functions.

By Fiscal Year, in Millions of Dollars												
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2009- 2013	2009- 2018
CHANGES IN SPENDING SUBJECT TO APPROPRIATION (On-Budget)												
Salary Payments and Other Discretionary Spending												
Estimated Authorization Level	35	117	181	175	170	167	164	163	163	163	677	1,498
Estimated Outlays	35	117	181	175	170	167	164	163	163	163	677	1,498
Employer Contributions ^a												
Estimated Authorization Level	17	51	78	78	80	82	84	88	90	93	304	741
Estimated Outlays	17	51	78	78	80	82	84	88	90	93	304	741
Total Changes in Spending Subject to Appropriation												
Estimated Authorization Level	52	168	259	253	250	249	250	251	253	256	981	2,239
Estimated Outlays	52	168	259	253	250	249	250	251	253	256	981	2,239
CHANGES IN DIRECT SPENDING (OUTLAYS)												
Total Changes in Direct Spending	2	7	13	21	28	35	42	47	52	56	71	302
On-Budget Spending	2	7	12	21	28	34	41	46	50	54	70	295
Off-Budget Spending	0	0	*	*	*	1	1	1	2	2	*	7
CHANGES IN REVENUES												
Total Changes in Revenues	24	70	106	105	109	112	116	119	123	127	415	1,011
On-Budget Revenues	19	54	82	81	84	86	89	91	94	97	321	778
Off-Budget Revenues	5	16	24	24	25	26	27	28	29	30	94	233
Memorandum:												
Total Intragovernmental Collections from Employer Contributions ^a	-17	-51	-78	-78	-80	-82	-84	-88	-90	-93	-304	-741
On-Budget	-12	-35	-54	-54	-55	-56	-57	-60	-61	-63	-210	-508
Off-Budget	-5	-16	-24	-24	-25	-26	-27	-28	-29	-30	-94	-233

Sources: Congressional Budget Office and Joint Committee on Taxation.

Notes: Components may not sum to totals because of rounding.

* = costs of less than \$500,000 annually.

a. Employer contributions are intragovernmental transactions that do not affect the deficit or surplus.

BASIS OF ESTIMATE

For this estimate, CBO assumes that S. 3013 will be enacted near the beginning of fiscal year 2009 and that the necessary amounts will be appropriated for each year. The bill would affect approximately 46,000 federal employees working in Alaska, Hawaii, Puerto Rico, the U.S. Virgin Islands, Guam, and the Northern Mariana Islands.

Currently, federal employees in those areas receive a COLA to offset higher costs of living in those areas. (In contrast, federal employees in the contiguous 48 states receive locality pay under the General Schedule to narrow the pay gap between comparable federal and non-federal positions.) S. 3013 would phase in the use of locality pay for employees in the specified areas over three years and would phase out the COLA, in most cases, over a longer period of time. Such changes would affect the federal budget because, while the COLA is not subject to federal income or payroll taxes and is not used to calculate federal retirement benefits, locality pay is both taxable and creditable for retirement benefits.

Spending Subject to Appropriation

S. 3013 would increase discretionary spending by \$2.2 billion over the 2009-2018 period, assuming the appropriation of necessary amounts, primarily for increased salary payments and agencies' payments for retirement benefits and payroll taxes.

Salary payments and other spending. Raising salaries for federal employees in the designated jurisdictions would result in \$1.5 billion in additional discretionary spending over the 2009-2018 period, CBO estimates.

The conversion to locality pay for approximately 38,000 eligible federal employees would increase salaries by \$1.5 billion over the next 10 years. For those employees, a provision in S. 3013 provides for a phase-out of COLAs over time, intended to preserve the take-home salaries of those employees as their non-taxable COLA pay is replaced with taxable locality pay. As a result, salaries would increase to maintain the take-home pay of affected employees.

A small amount of savings—\$2 million over 10 years—would result from discontinuing the surveys currently used by OPM to calculate the COLA adjustments for non-foreign areas.

Employer contributions. Similar to the rise in employees' contributions due to the transition to locality pay (which is creditable towards retirement), federal agencies' costs for payroll taxes and retirement contributions also would increase. Assuming appropriation of the necessary amounts, CBO estimates that spending for those contributions would increase

by \$741 million through 2018. Those payments are intragovernmental transactions that are recorded as offsetting receipts elsewhere in the budget.

Direct Spending

Increased retirement benefits (a product of increases in salaries) would accrue to approximately 13,000 federal employees anticipated to retire between 2009 and 2018. As a result, CBO estimates that direct spending would increase by a total of \$302 million over 10 years—\$295 million for additional retirement benefits and \$7 million for higher Social Security benefits.

Under S. 3013, an estimated 8,000 employees of the U.S. Postal Service (USPS) would not convert to locality pay and would continue to receive COLAs, but a provision of the bill would adjust the COLA calculation. If enacted, future calculations of COLAs for those employees would equal the greater of either the COLA in effect on December 31, 2008, or the locality pay applicable to other federal employees (that is, those who converted to locality pay under this bill) for that year and jurisdiction. CBO estimates that the provision could result in an increase in direct spending of about \$50 million (off-budget) over the 2009-2018 period. However, CBO assumes that any increase would be offset by additional receipts from postage rates charged by the USPS over the same period, and would have no net effect on the budget.

Revenues

S. 3013 would increase the portion of salary on which employees must pay taxes and would increase the amount of pay used to calculate employees' contributions for federal retirement benefits. Accordingly, the legislation would increase revenues by a total of \$1 billion over the next 10 years from additional income and payroll tax collections and from additional retirement contributions from employees, CBO and the Joint Committee on Taxation estimate. That total revenue change represents both on- and off-budget activity. Additional on-budget revenues would total \$778 million, including \$739 million from Medicare payroll taxes and income tax collections and \$39 million from higher contributions from employees toward retirement benefits. The increase in off-budget revenues would total \$233 million from additional Social Security tax receipts.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

S. 3013 contains no intergovernmental or private-sector mandates as defined in UMRA and would impose no cost on state, local, or tribal governments.

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